

Small Business Economic Impact Statement

Escrow Agents – Examination and Investigation Fees and Expenses WAC 208-680G-050

Industry Description

This proposal pertains to persons subject to licensure under the Escrow Agent Registration Act, Chap. 18.44 RCW. There are currently approximately 180 licensed Escrow Agents and 380 licensed Escrow Officers operating from approximately 210 locations.

Escrow Agent Registration Act – Chap. 18.44 RCW

The Escrow Agent Registration Act (“Act”) was enacted by the Legislature to protect escrow agent clients. “When read in its entirety, the Act reflects a legislative intent to protect clients of escrow agents.” *Estate of Jordan v. Hartford Accident & Indem. Co.*, 120 Wn.2d 490, 497 (1993). To that end, pursuant to RCW 18.44.410, the Director “has the power and broad administrative discretion to administer and interpret this chapter to facilitate the delivery of services to citizens of this state by escrow agents ... [and] may issue rules and regulations to govern the activities of licensed escrow agents and escrow officers.”

RCW 18.44.121(6) states that the Director shall charge an hourly audit fee and that in establishing fees, “the director shall set the fees at a sufficient level to defray the costs of administering this chapter.”

Summary of Proposed Amendment

WAC 208-680G-050, as adopted in 2001, provides in subsection (1) that the director may retain attorneys, CPAs, and other professionals as examiners or investigators at the expense of the person that is the subject of the examination or investigation. The current language in subsection (2) specifically provides that the expenses for required travel and services associated with an examination or investigation outside the state are to be borne by the person examined and investigated.

The current language is potentially misleading. Subsection (1) clearly authorizes reimbursement to DFI if it hires outside professionals and specialists, but is less clear when it comes to reimbursement of the costs of examinations by DFI examiners. Similarly, subsection (2) specifically allows the reimbursement of travel related expenses for out-of-state examinations, but is silent as to in-state examinations. The proposed amendments will clarify these possible ambiguities.

Subsection (2) would be amended to clearly state that examination and investigation related expenses are to be borne by the person examined or investigated, regardless of where that person is located. New Subsection (3) provides examples of the expenses for

which reimbursement may be owed and requires DFI to provide an invoice detailing such expenses at a reasonable time following the investigation or examination. Payment of the invoiced amount is due within 30 days of the invoice date.

Opportunity for Industry Involvement in Rulemaking

A CR-101 and a preliminary draft of the amended rule have been sent to all escrow agents and have been published on DFI's website. Copies have also been distributed and discussed at Escrow Commission meetings in October 2003, February 2004 and April 2004.

In April 2004, a survey was sent to all licensed escrow agents and published on DFI's website. The survey requested information concerning revenues, employees and other factors to be considered in the preparation of this SBEIS. Out of approximately 180 licensed escrow agents, 37 escrow agents responded to the survey. The preliminary results of that survey were discussed at the July 2004 Escrow Commission meeting.

DFI staff also met during the rule development process with State of Washington legislative staff. DFI discussed the proposed rule and received feedback from legislative staff about concerns raised by the escrow industry and possible ways to mitigate those concerns. As a final step prior to completion of the rule proposal, DFI met in August 2004 in Executive Session with members of the Escrow Commission, to discuss in detail several alternatives for implementation of the proposed rule and to assess the range of impacts that each alternative might have on the industry and individual escrow agents. These meetings resulted in significant changes to DFI's plan for implementation of the proposed rule. The proposed mitigation discussed at the end of this report was a direct result of these meetings and industry involvement.

Lost Sales or Revenues

The proposed amendments to WAC 208-680G-050 will not directly affect the relations between escrow agents and their customers. Therefore, loss of sales or revenues seems unlikely.

Costs of Compliance

Reporting and recordkeeping. The proposed amendments will not require increased reporting or recordkeeping.

Professional services. DFI does not believe that the proposed amendments will require escrow agents to retain additional professional services.

Equipment, supplies, labor, and administrative costs. DFI does not believe that the proposed amendments will require escrow agents to incur additional equipment, supplies, labor, or administrative costs.

Examination fees. DFI believes that the only significant costs of compliance resulting from these amendments will be the fees charged by DFI for examination of escrow agents. DFI will be reimbursed for the costs it incurs in examining escrow agents. Those costs consist primarily of the salaries, benefits, and other costs associated with supporting the two field examiners that perform the escrow agent examinations. DFI estimates those costs as follows:

Costs	Per Year	Notes
Salary	\$117,312	2 examiners @ Fin. Examiner 3 - midrange
Benefits	\$29,328	Calculated at 25% of salary
Travel	\$15,000	\$7,500 per examiner
Goods & Services	\$2,982	Cell phone, Blackberry, Wireless access
Total Cost	\$164,622	

Each examiner will perform an estimated 33 examinations per year (66 examinations total). DFI estimates that an average examination will take approximately one week and involve approximately 3 days onsite and 2 days for preparation, report writing, and follow-up. Generally, larger firms will take longer to examine than smaller companies. Using the one-week exam estimate, DFI's per exam cost is therefore approximately \$2,500 ($\$164,622 \div 66$) or \$62.50 per hour ($\$2,500 \div 40$).

The average exam cycle will be approximately 3.18 years (210 escrow agent locations \div 66 examinations per year), although DFI intends to employ a risk-based examination cycle under which the examination cycle for each particular escrow agent will vary from approximately yearly to once every seven years.

Survey and Mitigation

The Regulatory Fairness Act, RCW 19.85, requires an agency to assess whether the proposal will disproportionately impact "small business," which is defined as a business entity that has 50 or fewer employees. RCW 19.85.040(1) provides:

To determine whether the proposed rule will have a disproportionate impact on small businesses, the impact statement must compare the cost of compliance for small business with the cost of compliance for the ten percent of businesses that are the largest businesses required to comply with the proposed rules using one or more of the following as a basis for comparing costs:

- (a) Cost per employee;
- (b) Cost per hour of labor; or
- (c) Cost per one hundred dollars of sales.

RCW 19.85.030(2) further states:

Based upon the extent of disproportionate impact on small business identified in the statement prepared under RCW 19.85.040, the agency shall, where legal and feasible in meeting the stated objectives of the statutes upon which the rule is based, reduce the costs imposed by the rule on small businesses. Methods to reduce the costs on small businesses may include:

- (a) Reducing, modifying, or eliminating substantive regulatory requirements;
- (b) Simplifying, reducing, or eliminating recordkeeping and reporting requirements;
- (c) Reducing the frequency of inspections;
- (d) Delaying compliance timetables;
- (e) Reducing or modifying fine schedules for noncompliance; or
- (f) Any other mitigation techniques.

To gather the data necessary to comply with these statutes, DFI sent a survey to all licensed escrow agents on April 14, 2004. The survey was also published on DFI's website. By the return date of April 30, 2004, 37 escrow agents responded to the survey. None of the respondents had more than 50 employees. Therefore, all respondents are "small businesses." Since no respondent indicated that it was not a small business, DFI cannot perform the comparison described in RCW 19.85.040(1) and the agency is not required to reduce the costs imposed by the rule under 19.85.030(2). Nevertheless, DFI desires to minimize the impact of this proposal to the extent practicable. To that end a discussion of the survey results and DFI's plan to mitigate the impact of the rule follows.

Survey Results

A total of 37 escrow agents, operating 42 physical locations, responded to the survey. Some agents did not respond to all survey questions. The largest escrow agent responding to the survey had 37 employees and approximately \$3.8 million in revenue in 2003. The smallest respondent had approximately \$70,000 in 2003 revenue and one employee. The following table summarizes the results of the survey:

	Employees	2002 Revenue	2003 Revenue	2002 Income	2003 Income	2002 Closings	2003 Closings	Trust Accts	Open Escrow Accts
Company Average - Mean	5.27	\$517,494	\$637,759	\$107,689	\$158,174	842	1,052	1.39	153
Company Average - Median	4.00	\$379,294	\$417,659	\$50,160	\$46,510	700	750	1.00	66
Average per locat.	4.64	\$443,566	\$551,575	\$92,305	\$136,799	721	910	1.22	134

Observations

The small number of companies responding to the survey makes it difficult to draw firm conclusions regarding the industry. Nevertheless, from the survey results and its understanding of the industry, DFI makes the following observations:

- Due to historically low interest rates, 2002 and 2003 were high-volume years for the escrow industry.
- An exam fee of \$2,500 would constitute approximately 0.6% of 2003 median revenue. If the exam fee is annualized over the average exam cycle ($\$2,500 \div 3.33 \text{ years} = \$786/\text{year annualized}$) the percentage drops to 0.2% of 2003 median revenue.
- Escrow agents are routinely entrusted with large amounts of money and are typically regulated only by DFI.
- In light of the risks posed by the industry, the fees discussed above appear reasonable and affordable.
- Escrow agents have not been charged for examinations previously and some agents are concerned about the potential costs of such examinations.

Proposed Mitigation

DFI intends to institute the following mitigatory measures for the first year following the adoption of the rule:

- The hourly exam fee will be \$62.50 per hour.
- The exam fee will be charged only for the time the examiner is on site.

Mitigating the fees in this manner will be advantageous to escrow agents for the following reasons:

- An escrow agent will be in a position to verify the time for which the examiner was onsite. The agent will not be charged for exam time that it was not able to observe. Additionally, in not charging for off-site time, the total charge to the agent for examination will decrease, facilitating the ability of escrow agents to budget for this new cost.
- Escrow agents that are distant from Olympia will not be penalized by paying for actual travel costs.

Conclusion

Escrow agents handle millions of dollars on behalf of clients each year. DFI is typically the only entity regulating escrow agents. The Escrow Agent Registration Act was enacted to protect escrow agent clients. To effectively carry out this intent, it is necessary to have a robust field examination program. To that end, DFI has hired two dedicated, highly qualified escrow agent field examiners.

The proposed rule implements RCW 18.44.121(6), which requires the director to charge an hourly examination fee. Since examination fees have not been previously charged, the rule will have an economic impact on escrow agents. In response to the concerns raised by some agents, DFI will initially, as discussed above, mitigate the potential impact of the rule. While such mitigation is not required under Chap. 19.85 RCW, DFI understands the concerns that have been raised by some agents and believes that proposed mitigation will help address those concerns and further the relationship between DFI and the escrow industry.